

## Responses from P138 Assessment Consultation

Consultation issued 20 November 2003

Representations were received from the following parties:

No.	Company	File Number	No. BSC Parties Represented	No. Non-Parties Represented
1.	Innogy	P138_ASS_001	9	0
2.	Aquila Networks	P138_ASS_002	1	0
3.	British Gas Trading (BGT)	P138_ASS_003	1	0
4.	EDF Energy	P138_ASS_004	9	0
5.	National Grid Transco	P138_ASS_005	1	0
6.	Powergen	P138_ASS_006	14	0
7.	Scottish and Southern Energy	P138_ASS_007	4	0

**P138\_ASS\_001 – Innogy**

<b>Respondent:</b>	<i>Name</i> Bill Reed
<b>No. of BSC Parties Represented</b>	9
<b>BSC Parties Represented</b>	<i>Please list all BSC Parties responding on behalf of (including the respondent company if relevant).</i> Innogy plc, Innogy Cogen Limited, Innogy Cogen Trading Limited, Npower Limited, Npower Direct Limited, Npower Northern Limited, Npower Northern Supply Limited, Npower Yorkshire Limited, Npower Yorkshire Supply Limited
<b>No. of Non BSC Parties Represented</b>	
<b>Non BSC Parties represented</b>	<i>Please list all non BSC Parties responding on behalf of (including the respondent company if relevant).</i>
<b>Role of Respondent</b>	<i>(Supplier/Generator/ Trader / Consolidator / Exemptable Generator / BSC Agent / Party Agent / other – please state <sup>1</sup>)</i> Supplier/Generator/ Trader / Consolidator / Exemptable Generator / Party Agent

<b>Q</b>	<b>Question</b>	<b>Response <sup>1</sup></b>	<b>Rationale</b>
1.	Do you believe Proposed Modification P138 better facilitates the achievement of Applicable BSC Objective (b) The efficient, economic and co-ordinated operation by the Transmission Company of the Transmission System?	Yes	As noted in our Modification Proposal “The proposal will better facilitate Objective (b) in relation to the efficient, economic and co-ordinated operation by the Transmission Company of the Transmission System by ensuring that Demand Control periods can be effectively utilised under the BSC. Furthermore, the proposal will introduce appropriate incentives on NGC to ensure that the cost of demand control is appropriately targeted.”

---

<sup>1</sup> Please delete as appropriate.

Q	Question	Response <sup>1</sup>	Rationale
2.	Do you believe Proposed Modification P138 better facilitates the achievement of Applicable BSC Objective (c) Promoting effective competition in the generation and supply of electricity, and (so far as consistent therewith) promoting such competition in the sale and purchase of electricity?	Yes	As noted in our Modification Proposal "By treating demand control as a BM action and removing the potential financial risks associated with Demand Control measures, the proposal will better facilitate Objective (c) of the BSC in relation to the promotion of effective competition in the generation and supply of electricity, and (so far as consistent therewith) promoting such competition in the sale and purchase of electricity. Specifically the proposal will remove the risk that parties are exposed to high and unpredictable imbalance charges and residual cashflow reallocation cashflows during a Demand Control Period."
3.	Do you believe Proposed Modification P138 has a negative impact on Applicable BSC Objective (d) Promoting efficiency in the implementation and administration of the balancing and settlement arrangements	No	There are currently no contingency arrangements associated with demand control periods in the BSC. The proposal will address this defect and on this basis will better facilitate Objective (d) by promoting efficiency in the implementation and administration of the balancing and settlement arrangements
4.	Overall, do you believe Proposed Modification P138 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state objective(s)	Yes	The proposal better facilitates Objectives (b) and (c) for the reasons stated above, and may also better facilitate Objective (d).
5.	Do you support the implementation approach described in the consultation document / the implementation option preferred by the Modification Group? Please give rationale	Yes	A solution based on the lowest cost of implementation is appropriate since it is difficult to justify major system changes to accommodate a rare event.
6.	Do you believe there are any alternative solutions that would better facilitate the Applicable BSC Objectives to a greater degree than P138 (for example, adopting P138 with one of the suggested alternative pricing options or any other options that the Modification Group has not identified) that should be considered? Please give rationale	No	

Q	Question	Response <sup>1</sup>	Rationale
7.	Do you agree with the PSMG's views of the scope of P138 in relation to those Parties covered / not covered by the modification (see page 3 of the consultation document)? Please give rationale	Yes	Demand control based on Grid Code OC6 transmission operator instructed events impacts on supplier BMUs.
8.	Does P138 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	No	
9.	Are there any further comments on P138 that you wish to make?	No	

**P138\_ASS\_002 – Aquila Networks**

Hello,

Please find that there is no impact to Aquila Networks Plc systems and/or processes.

regards

Rachael Gardener

**P138\_ASS\_003 – British Gas Trading**

<b>Respondent:</b>	Mark Manley
<b>No. of BSC Parties Represented</b>	
<b>BSC Parties Represented</b>	British Gas Trading (BGT)
<b>No. of Non BSC Parties Represented</b>	
<b>Non BSC Parties represented</b>	
<b>Role of Respondent</b>	

<b>Q</b>	<b>Question</b>	<b>Response <sup>1</sup></b>	<b>Rationale</b>
1.	Do you believe Proposed Modification P138 better facilitates the achievement of Applicable BSC Objective (b) The efficient, economic and co-ordinated operation by the Transmission Company of the Transmission System?	No	BGT believe that this modification will have a negligible impact on the behaviour of the System Operator (SO) in maintaining an economic, efficient and co-ordinated Transmission System. BGT do not concur with the view that this will send the correct price signals to market participants to incentivise balance. The amendment to the imbalance price will be retrospective and as such will not provide a real time price signal that BSC Parties will be able to respond to.

Q	Question	Response <sup>1</sup>	Rationale
2.	Do you believe Proposed Modification P138 better facilitates the achievement of Applicable BSC Objective (c) Promoting effective competition in the generation and supply of electricity, and (so far as consistent therewith) promoting such competition in the sale and purchase of electricity?	Yes	<p>BGT believe P138 will better facilitate effective competition in the sale and generation of electricity. There is a defect within the current methodology, which may benefit the party that caused the problem to the detriment of a party that attempted to balance their position. P138 will amend this to ensure all Parties contract positions are reflective of their notified position prior to demand control being initiated.</p> <p>BGT also supports removing the ability of the SO to call demand control and not paying for the instruction. BGT is unsure if the payment should be based upon a marginal action or if it more appropriate for the repayment to be based on the reverse price.</p> <p>BGT believes any solution should ensure that the volume associated with the demand control instruction is feed back into the derivation of the imbalance price. This will ensure that the NIV tagging process is more robust as it will be more accurate and it will also ensure that the energy imbalance price is more reflective of the actions taken by the SO.</p>
3.	Do you believe Proposed Modification P138 has a negative impact on Applicable BSC Objective (d) Promoting efficiency in the implementation and administration of the balancing and settlement arrangements	No	BGT agree that the modification adds cost and complexity to the processing of settlements and therefore this modification will be to the detriment of Applicable BSC Objective (d).
4.	Overall, do you believe Proposed Modification P138 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state objective(s)	Yes	Whilst BGT do not believe Applicable BSC Objective (b) will be better facilitated similarly BGT do not believe it will be adversely impacted either. BGT note the detrimental effect on Applicable BSC Objective (d) but believe these to be outweighed by the benefits associated with Objective (c).

Q	Question	Response <sup>1</sup>	Rationale
5.	Do you support the implementation approach described in the consultation document / the implementation option preferred by the Modification Group? Please give rationale	Yes	BGT support the implementation approach outlined by the Modification Group. The solution should have minimal system impact and it should be inexpensive to implement. If this is not the case the downside of Objective (d) could outweigh the benefits provided under Objective (c).
6.	Do you believe there are any alternative solutions that would better facilitate the Applicable BSC Objectives to a greater degree than P138 (for example, adopting P138 with one of the suggested alternative pricing options or any other options that the Modification Group has not identified) that should be considered? Please give rationale	No	
7.	Do you agree with the PSMG's views of the scope of P138 in relation to those Parties covered / not covered by the modification (see page 3 of the consultation document)? Please give rationale	Yes	BGT support the scope of the modification in terms of the Parties covered by the solution.
8.	Does P138 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	No	
9.	Are there any further comments on P138 that you wish to make?	No	



**P138\_ASS\_004 – EDF Energy**

<b>Respondent:</b>	Tony Dicicco
<b>No. of BSC Parties Represented</b>	9
<b>BSC Parties Represented</b>	EDF Energy Networks (EPN) plc; EDF Energy Networks (LPN) plc EDF Energy Networks (SPN) plc; EDF Energy (Sutton Bridge Power) EDF Energy (Cottam Power) Ltd; EDF Energy (West Burton Power) Ltd; EDF Energy plc; London Energy plc; Seeboard Energy Limited
<b>No. of Non BSC Parties Represented</b>	0
<b>Non BSC Parties represented</b>	N/A
<b>Role of Respondent</b>	Supplier/Generator/ Trader

<b>Q</b>	<b>Question</b>	<b>Response</b>	<b>Rationale</b>
1.	Do you believe Proposed Modification P138 better facilitates the achievement of Applicable BSC Objective (b) The efficient, economic and co-ordinated operation by the Transmission Company of the Transmission System?	Yes	EDF Energy do recognise that Demand Control is an instruction issued to meet energy requirements, and we believe that Suppliers should be paid for demand shed under OC6. We also recognise that Demand Control is a rare event and often a last resort decision. We believe that introducing a price for Demand Control similar to other Balancing Mechanism actions will lead to the efficient and economic running of the Transmission System by the Transmission Company.
2.	Do you believe Proposed Modification P138 better facilitates the achievement of Applicable BSC Objective (c) Promoting effective competition in the generation and supply of electricity, and (so far as consistent therewith) promoting such competition in the sale and purchase of electricity?	Yes	EDF Energy believe that importing Supplier BM Units in a GSP Group affected by Demand Control should not be exposed to increased imbalance exposure because of such an instruction. We believe that P138 would promote competition by removing this exposure.

Q	Question	Response	Rationale
3.	Do you believe Proposed Modification P138 has a negative impact on Applicable BSC Objective (d) Promoting efficiency in the implementation and administration of the balancing and settlement arrangements	No	EDF Energy believe that the costs associated with implementing a manual solution for P138 do not have a negative impact on facilitating Applicable BSC Objective (d).
4.	Overall, do you believe Proposed Modification P138 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state objective(s)	Yes	EDF Energy believe that importing Supplier BM Units should be compensated for Demand Control instructions and with sight of the total costs EDF Energy believe that P138 will better facilitate achievement of the Applicable BSC Objectives.
5.	Do you support the implementation approach described in the consultation document / the implementation option preferred by the Modification Group? Please give rationale	Yes	EDF Energy believe that pricing a Demand Control Offer from the highest priced accepted Offer, that has not been tagged out, in the first Settlement Period in which Demand Control is instructed is the appropriate implementation option.
6.	Do you believe there are any alternative solutions that would better facilitate the Applicable BSC Objectives to a greater degree than P138 (for example, adopting P138 with one of the suggested alternative pricing options or any other options that the Modification Group has not identified) that should be considered? Please give rationale	No	
7.	Do you agree with the PSMG's views of the scope of P138 in relation to those Parties covered / not covered by the modification (see page 3 of the consultation document)? Please give rationale	Yes	EDF Energy believe that the proposed solution covers Supplier BM Units who do not usually participate in the BM. As stated in the consultation document directly connected BM Units are more likely to be BM participants and can give economic signals to the System Operator.

Q	Question	Response	Rationale
8.	Does P138 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	No	
9.	Are there any further comments on P138 that you wish to make?	Yes	It is unfortunate that the impact assessments were not available at the start of the P138 consultation. EDF Energy believe that as the frequency of demand control is rare we would want the costs to be kept to a minimum, i.e. manual processes where possible. Without the impact assessments it would have been difficult to determine whether P138 better facilitates achievement of the Applicable BSC Objectives.

**P138\_ASS\_005 – National Grid Transco**

<b>Respondent:</b>	<i>National Grid Transco</i>
<b>No. of BSC Parties Represented</b>	<i>1</i>
<b>BSC Parties Represented</b>	<i>National Grid Company</i>
<b>No. of Non BSC Parties Represented</b>	<i>0</i>
<b>Non BSC Parties represented</b>	<i>0</i>
<b>Role of Respondent</b>	<b>Transmission System Operator</b>

<b>Q</b>	<b>Question</b>	<b>Response <sup>1</sup></b>	<b>Rationale</b>
1.	Do you believe Proposed Modification P138 better facilitates the achievement of Applicable BSC Objective (b) The efficient, economic and co-ordinated operation by the Transmission Company of the Transmission System?	<b>No</b>	See Below
<p><b>Economic Incentive on the Transmission System Operator to avoid Demand Control</b></p> <p>P138 states that National Grid currently has a perverse option to initiate Demand Control under OC6 as a ‘free’ option, thus suggesting that there is a higher probability of Demand Control being exercised. If Demand Control was an option available to National Grid as a balancing service that could be utilised based upon economic rationale, then it would be right and proper that Demand Control were priced and in doing so, Applicable BSC Objective (b) would be better facilitated.</p> <p>However, Demand Control as instructed under OC6 of the Grid Code is <b>NOT</b> an option open to National Grid based upon economic rationale. If it were, National Grid would have made use of it as a justifiable balancing service long before now. The very fact that National Grid has not instructed Demand Control for such a long time clearly indicates that it is not seen as a ‘free’ option and is treated as an action to be ‘avoided at all costs’. Charging National Grid for taking Demand Control will have no impact upon its behaviour. Demand Control will occur whether or not there is a cost associated with it. National Grid would take every feasible action, irrespective of price, prior to initiating Demand Control.</p>			

Demand Control is an operational decision taken as a result of either insufficient contracted reserve or failure the of the market to provide sufficient energy to meet demand. The level of contracted reserve is driven by National Grid's obligations in relation to Security of Supply. Putting a price on Demand Control, as suggested under P138, will not impact the level of reserve held and will do nothing to prevent insufficient generation being contracted by suppliers and the market failing. It will, as a result, fail to lead to the more efficient, economic or co-ordinated operation of the Transmission System. National Grid should not be penalised following the failure of the market over which it has limited control.

If the assertion, made by the proposer of P138, that National Grid will respond to the pricing of Demand Control is correct (a point strongly refuted by National Grid), then there could be a perverse incentive making it more likely that Demand Control is initiated. The modification proposes that National Grid pay for Demand Control at the marginal price. The Marginal Price is defined as the highest priced offer taken prior to the initiation of Demand Control. This could incentivise National Grid to take Demand Control earlier than would otherwise have been the case, as the earlier it is initiated, the cheaper it will be. If this incentive is taken to its logical conclusion, Demand Control will be the first action taken by National Grid as it will be 'free' due to the fact that there is no offer price to set the cost of the action. Based upon this logic P138 fails to achieve its objective of making Demand Control less likely.

Based upon the same incorrect premise that National Grid will respond to the costing of Demand Control, it could be argued that National Grid would never take Demand Control, preferring to wait until the system begins to collapse in an uncontrolled manner and a Black Start situation occurs. This would avoid the need for National Grid to pay for the action at the prevailing marginal price as proposed by P138, but would obviously be an undesirable outcome for the wider industry and an inappropriate incentive for National Grid.

#### **Sharpened incentive to balance through increased imbalance prices**

The inclusion of deemed Demand Control Offers (at a marginal offer price) within the offer stack used to calculate imbalance prices (SBP/SSP), could lead to an increase in average SBP and thus supposedly increase the incentive on parties to balance. Whilst National Grid agrees with the principle of improving incentives on parties to balance, especially at times of system stress, it is believed that there are more appropriate means of achieving this (e.g. P136/P137). Imbalance Prices are only increased under P138 as a result of National Grid paying suppliers what is effectively a 'windfall' payment following Demand Control. This windfall payment may reduce incentives on suppliers to balance as it would reduce or negate any increase in imbalance cost exposure faced by suppliers who are in a 'short' contracted position. Without the perversions associated with windfall payments, the sharper incentives on parties' to balance would better facilitate Applicable BSC Objective (b). Unfortunately, the increase in imbalance prices is directly linked to the payment of such windfall gains.

**Transmission Company Payment following an action that could have been avoided by the market more efficiently**

National Grid believes that payment at a marginal price, by the System Operator, for Demand Control volume is in direct contradiction to Applicable BSC Objective (b) as it would almost certainly have been more efficient for the energy to be procured through forward contracts to ensure that sufficient was made available. If Demand Control is required due to a lack of available energy to meet demand, the market should be incentivised to contract for greater volumes. It can readily be assumed that the cost per MW of such contracting would be less than the marginal offer price P138 suggests is paid for every MW of demand reduced.

**Previous industry views relating to sharper imbalance prices at times of Demand Control**

Whilst not fully agreeing with the views made by industry participants in relation to P135, National Grid notes that the same counter arguments could be applied to the changes to imbalance prices and the signals provided to the market as a result of P138.

As with P135, it appears obvious that the P138 proposal would lead to increased uncertainty in relation to imbalance prices and Residual Cashflow Reallocation Cashflow (RCRC) payments at times of Demand Control. Under the proposal, the increase in imbalance prices, and resultant RCRC payments, would be dependent upon the volume associated with, and price at which, Demand Control is instructed. Neither the volume nor price, associated with the Demand Control action under P138, is predictable. As such, P138 will lead to increased uncertainty within the market.

Another argument against P135 was the inappropriate nature of post event calculations to determine cashout prices. National Grid notes that the proposed P138 mechanism relies upon post event calculation and allocation of volumes, identification of prices and calculation of payments. This means that prompt pricing becomes impossible during a Demand Control Period, a requirement that has previously been held as sacrosanct by market participants during other pricing modification discussions.

Similarly, market participants have previously indicated that pricing signals that only present themselves at times of Demand Control, come too late to affect behaviour as they are only seen after the event and can not be predicted. As such, higher imbalance prices that only occur following Demand Control will have no impact upon the contracting behaviour of industry participants.

National Grid further notes that it could be suggested that the P138 modification proposal results in the need for the development of a separate pricing regime that only operates at times of Demand Control. As industry participants have previously argued, this could be seen to be inefficient and to inappropriately introduce unnecessary complexity and uncertainty into the market.

If the above views expressed by other industry participants are valid, P138 clearly fails to better facilitate Applicable BSC Objective (b).

2.	Do you believe Proposed Modification P138 better facilitates the achievement of Applicable BSC Objective (c) Promoting effective competition in the generation and supply of electricity, and (so far as consistent therewith) promoting such competition in the sale and purchase of electricity?	<b>No</b>	See Below
----	--	-----------	-----------

**Treatment of volume associated with Demand Control**

National Grid recognises that, under current arrangements, Suppliers' incentives to balance are dampened at times of Demand Control as the resultant reduction in metered volumes will generally improve affected Suppliers' imbalance positions. By treating Demand Control volumes as deemed offers, suppliers' contracted positions are changed such that their imbalance positions are not impacted by the Demand Control action. National Grid fully supports the removal of the current perversion that could reduce incentives on suppliers to balance at times of Demand Control. In this way, P138 does better facilitate Applicable BSC Objective (c).

In most cases P138 will appropriately account for the impact of Demand Control on Suppliers' contracted volumes. However, National Grid notes that this may not be the case where Demand Control is effected by disconnecting specific loads. In such a situation it will be quite clear which Supplier's metered volume will have been affected and which Supplier should receive the Demand Control Offer payment. However, the proposed P138 mechanism does not take account of this, effectively smearing the reduced volume across the whole Supplier community based upon their market shares within the GSP Group. This results in Demand Control Offer payments being made to Suppliers that were not affected by the Demand Control action, whilst the Supplier that lost significant metered volume will only receive a small element of the total Demand Control Offer payment that should have been received under the principles of P138.

Despite the acceptance that, in most cases, P138 appropriately accounts for the impact of Demand Control on Suppliers' contracted volumes, National Grid believes that other elements of P138 counteract the benefits of correctly accounting for the volumes associated with Demand Control resulting in an overall detrimental impact on Applicable BSC Objective (c).

**Windfall Payments to Suppliers at times of Demand Control**

National Grid believe it wholly inappropriate for Suppliers to be rewarded with, what equates to, a 'windfall' payment in the event of Demand Control. If payment is made at the Marginal Offer Price taken within the BM, this could provide perverse incentives on Suppliers as they will benefit when there is Demand Control. This can clearly be seen in the examples contained within the consultation document.

**Increased costs for all parties through BSUoS charges**

National Grid note that payment for deemed offers associated with Demand Control will be re-charged to the industry through BSUoS. BSUoS charges reflect the costs incurred by National Grid in balancing the system. The re-allocation of P138 costs through BSUoS charges results in parties not impacted



by Demand Control paying for the windfall payments received by parties that are affected by Demand Control. Payment for Demand Control through BSUoS is based upon the total metered volumes of all market participants and has no relation to whether a party has contributed to the Demand Control initiation through their imbalance position. National Grid does not believe that it is appropriate for a Supplier to benefit from Demand Control, at the expense of other parties within the industry, when it could have been in a 'short' position and thus contributing to the need for Demand Control to be initiated.

The allocation of BSUoS charges is based upon metered volumes. As such National Grid further notes that ironically, those suppliers benefiting from windfall payments as a result of having their metered volumes reduced, will also benefit from reduced BSUoS, TNUoS and possibly DUoS charges, as these are all calculated as a factor of metered volume that will reduce following Demand Control. The recovery of total costs by National Grid is achieved through the general socialisation of costs across the community. Whilst affected suppliers benefit through reduced metered volumes, non-affected parties will face higher costs as their market share is artificially increased, seeing them incur a higher proportion of charges.

#### **Barrier to entry for Smaller Suppliers**

National Grid notes that the impact of increased BSUoS charges being incurred by all industry participants whilst payment following Demand Control being made to a limited number of suppliers based upon their metered volumes in a specific area, will discriminate against smaller suppliers. Smaller suppliers, or suppliers whose customer base is locational specific, are proportionately less likely to receive payment following demand control, but guaranteed to pay a proportional increase in BSUoS charges. This effect is in direct contradiction of Applicable BSC objective (c).

#### **Re-allocation of monies around the industry**

The eight examples, contained within the consultation document, clearly demonstrate that the net impact upon industry participants resulting from cashflows associated with P138 is completely arbitrary. The range of different volumes, prices, imbalance positions etc. that can be in place when Demand Control occurs means that no single party can be certain of being better or worse off. As a result, P138 is unlikely to change the behaviour of any participant. Demand Control will thus be just as likely to occur if P138 is approved as it is now. The modification provides no clear incentives that will change the behaviour of Generators or Suppliers from that that they currently display. As stated in response to question 1, the modification will have no impact upon the behaviour of National Grid.

From the examples contained within the consultation document, it can quite clearly be seen that, whilst generators are generally made worse off by P138 as a result of facing higher BSUoS charges without benefiting from any windfall payments, there could be situations where they benefit as a result of the increase in Residual Cashflow Reallocation Cashflow (RCRC) payments being greater than the increased BSUoS charges.

Similarly, Suppliers not affected by Demand Control (e.g. Supplier B) are generally worse off as a result of being subject to higher BSUoS costs without benefiting from payment for reduced volumes. However, these suppliers too could be made better off under P138 if RCRC payments outweigh the increased BSUoS charges.

In all examples Supplier C is contributing to the need for Demand Control by being in a 'short' contracted position. Despite this 'short' position, in the majority of examples (5 out of 8), Supplier C is made better off following Demand Control under P138. This appears to provide a perverse incentive whereby Suppliers who contribute to the need for Demand Control could benefit from its instruction.

The re-allocation of monies resulting from P138 fails to provide any incentive on industry parties to change behaviours from those currently displayed. As such P138 fails to better facilitate BSC Applicable Objective (c).

In summary, P138 seems to provide a windfall payment to affected Suppliers resulting in a seemingly haphazard re-allocation of costs around the community.

3.	Do you believe Proposed Modification P138 has a negative impact on Applicable BSC Objective (d) Promoting efficiency in the implementation and administration of the balancing and settlement arrangements	<b>Yes (has a negative impact &amp; does not better facilitate)</b>	See Below
----	--	---	-----------

The process associated with the implementation and administration of the changes proposed by P138 has been hugely simplified. As a result of the necessary simplification of the procedures proposed to effect the P138 objectives, estimates are used to calculate other estimates, which in turn determine potentially significant changes in industry cash flows resulting in a lottery of P138 winners and losers.

P138 not only simplifies the proposed process through the use of estimates to drive key calculations, but also simplifies those calculations by making the assumption that some parties will not be impacted by Demand Control (e.g. embedded generators and directly connected customers). Whilst the logic used to justify their exclusion may be right in some cases, there may be times when P138 discriminates against such parties as a result of their exclusion.

The process proposed under P138 will add significant complexity to the implementation and administration of the balancing and settlement arrangements. As well as this increased complexity, it will also add uncertainty and increase risk for parties operating within the industry. There will be significantly different BSUoS charges, Imbalance prices and RCRC payments as a result of P138 and parties will have to wait until 48+ hours after the end of each Demand Controlled settlement period before knowing the impact that the P138 calculations will have on them and on parties that they trade with. The information required to determine the effect of P138 cashflows on any given party will not be available prior to the completion of the Initial Settlement Run.

Where a change to the process of managing the balancing and settlement arrangements results in the inability to provide prompt prices, increased uncertainty and volatility, greater scope for error, increased costs and a risk of discrimination, it can not better facilitate Applicable BSC Objective (d).

4.	Overall, do you believe Proposed Modification P138 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state objective(s)	<b>No</b>	See Below
----	---	-----------	-----------

The only aspect of P138 that better facilitates any of the Applicable BSC Objectives is the treatment of Demand Control Volumes that removes the perversity of making Suppliers better off following Demand Control as a result of the resultant effect on metered volumes and imbalance positions.

This benefit of P138 is more than out weighed by the detrimental impact that the modification would have on Applicable BSC Objectives b, c and d.

**In summary, Applicable BSC Objective (b) is made worse by:**

- Requiring the System Operator to pay for an action that may have been avoided more efficiently by market participants;
- Increasing System Operator costs and thus BSUoS charges without changing behaviour or making Demand Control a less likely event;
- Potentially making either Demand Control or a blackout situation a more likely event;
- Increasing the risk of high and unpredictable Imbalance and RCRC payments; and
- Making windfall payments to suppliers that could lead to perverse incentives and increase the costs incurred in balancing the system.

**Applicable BSC Objective (c) is made worse by:**

- Restricting competition by creating a potential barrier to entry for smaller Suppliers;
- Inappropriately rewarding suppliers with windfall payments following Demand Control, potentially reducing incentives for suppliers to contract appropriately;
- Increasing costs for all industry participants through higher BSUoS charges; and
- Creating a lottery of winners and losers that has no bearing upon the effectiveness of a party's contracted position.

**Applicable BSC Objective (d) is made worse by:**

- Making high level assumptions and basing key calculations upon estimates rather than actual data;
- Increasing system and administration costs without positively changing behaviours or making Demand Control less likely;
- Increasing market uncertainty and volatility through unpredictable cash flows and delays in providing associated market information;
- Failing to feed Demand Control prices and volumes into Prompt Pricing calculations; and
- Creating a risk of inappropriately dealing with embedded generators and directly connected customers.

5.	Do you support the implementation approach described in the consultation document / the implementation option preferred by the Modification Group? Please give rationale	<b>Yes (with reservations)</b>	See Below
<p>Taking into account the fact that Demand Control is unlikely to occur very often, National Grid generally supports the proposal that “there should be minimal system impact form this proposal...”</p> <p>However, whilst not disagreeing with the pragmatic approach being taken in using estimates to determine the impact of Demand Control on Suppliers’ metered volumes, it does have concerns that these very high level estimates will be used to determine what could be significant cashflows. The accuracy of the volume estimates will not only determine Demand Control Offer payments, but will affect imbalance volumes, Imbalance payments and RCRC payments. A small error in the volume estimates could result in disproportionate impacts upon cashflows and the monies paid by and to each individual party. The fact that the total Demand Control volume is based upon a high level estimate provided by the Distribution System Operator and is then allocated to suppliers based upon an estimated market share derived from volumes taken from a completely different period, reinforces the fact that cashflows associated with P138 are little more than a lottery.</p>			
6.	Do you believe there are any alternative solutions that would better facilitate the Applicable BSC Objectives to a greater degree than P138 (for example, adopting P138 with one of the suggested alternative pricing options or any other options that the Modification Group has not identified) that should be considered? Please give rationale	<b>Yes</b>	See below

National Grid has already explained in its response to questions 1 to 4 that, other than the lack of any current means of accounting for the volume associated with Demand Control, it does not believe that the defects assumed by P138 exist. In considering whether there is an alternative to P138 that better facilitates the Applicable BSC Objectives, it can only look at an alternative that treats the volume associated with Demand Control whilst reducing, or removing, the aspects of the modification that have a detrimental impact upon the BSC Objectives. In this respect, all of the alternative means of pricing the Demand Control Action better facilitate the BSC Objectives due to the fact that they result in a scaled reduction in the detrimental impact that the main proposal has. Any alternative means of pricing the Demand Control volume is better than the original modification.

#### **Option of a Zero Price for the Demand Control Offer Price**

By setting the Demand Control Offer Price to zero, the modification will effectively put Suppliers' imbalance volumes back to the levels faced prior to the Demand Control action. This will be achieved without the detrimental affects of windfall payments, higher BSUoS payments, perverse incentives on Suppliers and the System Operator, or barriers to entry that are a characteristic of the main modification proposal.

National Grid supports the development of an alternative to the main P138 proposal that has a zero value for the Demand Control Offer Price. However, it notes that the rules around tagging will have to be carefully considered as the inclusion of the Demand Control volume in the Offer stack at a zero price could have the negative effect of depressing average SBP. This would obviously be undesirable as at times of system stress, incentives on parties to balance should be at their greatest. Any dampening of SBP would be undesirable.

7.	Do you agree with the PSMG's views of the scope of P138 in relation to those Parties covered / not covered by the modification (see page 3 of the consultation document)? Please give rationale	<b>Yes (with reservations)</b>	See Below
----	--	--------------------------------	-----------

National Grid supports the PSMG's view of the scope of P138 in that it provides a pragmatic and simple approach of implementing the proposal without incurring significant cost or requiring complex calculations to cover an event that is unlikely to occur on a frequent basis. However, it does have concerns that the potential size of Demand Control payments and increases in BSUoS charges etc. could discriminate against direct connected and embedded Generators in some circumstances.

8.	Does P138 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	<b>Yes</b>	See Below
<p>National Grid believes that the PSMG should ensure that there is an agreed understanding as to how the tagging mechanism will work following Demand Control in a post P138 environment. There is clearly a risk that the Demand Control offer could be tagged out as a result of CADL or De-minimus tagging. This will obviously dampen any incentive on parties to balance by reducing the imbalance charges faced by those parties out of balance and contributing to the need for Demand Control to be initiated.</p>			
9.	Are there any further comments on P138 that you wish to make?	<b>Yes</b>	See Below
<p>National Grid Notes that the Business Requirements Specification and the P138 Mechanism documents indicate that, following initiation of Demand Control, the System Operator is expected to provide details of the affected GSP group(s), the affected LDSO(s), the amount of Demand Control requested as both a percentage reduction and actual volume. At the point of initiation, the System Operator will not know which GSP Group(s) is affected as it will instruct Demand Control from a Local Distribution System Operator (LDSO) and leave the LDSO to decide how and where the instruction is delivered. Similarly, at the point of instruction, the System Operator will ask an LDSO to deliver stage one Demand Control. This will reflect a percentage reduction in demand, across the LDSO's network, of between 4 and 6 percent in line with their submission to the Transmission System Operator on an annual basis. The System Operator will not ask for a specific volume of Demand Control to be delivered. As a result of the limited information available at the point of initiation, the System Operator will only be able to confirm the start time and details of which LDSO has been asked to initiate Demand Control under OC6.</p> <p>Immediately following the instruction to an LDSO to reconnect demand, the System Operator may not know or be able to estimate the volume of demand reduced as part of the Demand Control instruction. As such it may be difficult to provide an estimate of the reduced volume delivered by the Demand Control action until some time after the notice is published detailing the end time of the Demand Control period.</p>			

**P138\_ASS\_006 – Powergen**

<b>Respondent:</b>	Powergen
<b>No. of BSC Parties Represented</b>	14
<b>BSC Parties Represented</b>	Powergen UK plc, Powergen Retail Limited, Cottam Development Centre Limited, TXU Europe Drakelow Limited, TXU Europe Ironbridge Limited, TXU Europe High Marnham Limited, Midlands Gas Limited, Western Gas Limited, TXU Europe (AHG) Limited, TXU Europe (AH Online) Limited, Citigen (London) Limited, Severn Trent Energy Limited (known as TXU Europe (AHST) Limited), TXU Europe (AHGD) Limited and Ownlabel Energy Limited
<b>No. of Non BSC Parties Represented</b>	-
<b>Non BSC Parties represented</b>	-
<b>Role of Respondent</b>	Supplier, Generator, Trader & Exemptable Generator.

<b>Q</b>	<b>Question</b>	<b>Response</b>	<b>Rationale</b>
1.	Do you believe Proposed Modification P138 better facilitates the achievement of Applicable BSC Objective (b) The efficient, economic and co-ordinated operation by the Transmission Company of the Transmission System?	No	Even though treating the amount of demand reduction as an offer appears the correct intellectual thing to do, it is not clear that it will send a sufficient signal to participants to improve balancing or to ensure sufficient plant is available. The proposal suffers from the same problem as P135. That is, the signal will be sent too late, as it comes once the event has actually occurred. It is possible for imbalance prices to send signals to participants when past imbalance prices alter expectations of likely future levels. However, this mechanism will be used infrequently meaning that participants will have insufficient experience of the relevant prices for it to alter their future expectations.



Q	Question	Response	Rationale
2.	Do you believe Proposed Modification P138 better facilitates the achievement of Applicable BSC Objective (c) Promoting effective competition in the generation and supply of electricity, and (so far as consistent therewith) promoting such competition in the sale and purchase of electricity?	No	It is not clear that the present treatment of demand control is acting as a deterrent to competition in supply.
3.	Do you believe Proposed Modification P138 has a negative impact on Applicable BSC Objective (d) Promoting efficiency in the implementation and administration of the balancing and settlement arrangements	Yes	It will increase the complexity of the price setting arrangements.
4.	Overall, do you believe Proposed Modification P138 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state objective(s)	No	On balance, we do not believe that the potential benefits in terms of the small increase in intellectual purity of the arrangements are worth the increase in complexity in the price setting arrangements.
5.	Do you support the implementation approach described in the consultation document / the implementation option preferred by the Modification Group? Please give rationale	No	
6.	Do you believe there are any alternative solutions that would better facilitate the Applicable BSC Objectives to a greater degree than P138 (for example, adopting P138 with one of the suggested alternative pricing options or any other options that the Modification Group has not identified) that should be considered? Please give rationale	No	

Q	Question	Response	Rationale
7.	Do you agree with the PSMG's views of the scope of P138 in relation to those Parties covered / not covered by the modification (see page 3 of the consultation document)? Please give rationale	Yes	
8.	Does P138 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale	No	
9.	Are there any further comments on P138 that you wish to make?	No	

## **P138\_ASS\_007 – Scottish and Southern Energy**

Dear Sirs,

This response is sent on behalf of Scottish and Southern Energy, Southern Electric, Keadby Generation Ltd., SSE Energy Supply Ltd. and Medway Power Ltd.

In relation to the nine questions listed in the Consultation Paper, contained within your note of 10th November 2003 concerning Modification Proposal P138, we have the following comments to make:-

Q1 Do you believe Proposed Modification P138 better facilitates the achievement of Applicable BSC Objective (b) The efficient, economic and co-ordinated operation by the Transmission Company of the Transmission System?

No. Demand Control is (and should remain) a purely operationally driven decision taken by the SO to ensure the overall system stability and implemented via Emergency Instructions. It is not a 'commercial' decision taken by the SO (such 'commercial' decisions being taken by the SO via the other means such as the BM, PGBTs etc.).

In this respect we fundamentally oppose any suggestion that "the SO should be financially incentivised not to use it" as this implies (if the incentive is not 'sufficient') that the SO might consider (from a financial / commercial perspective) to invoke Demand Control. In the very rare event that Demand Control is used it should only be utilised to ensure the overall stability of the system. In this respect the SO should only

consider the technical aspect of maintaining the integrity of the system and should not take account of any financial consideration.

Q2 Do you believe Proposed Modification P138 better facilitates the achievement of Applicable BSC Objective (c) Promoting effective competition in the generation and supply of electricity, and (so far as consistent therewith) promoting such competition in the sale and purchase of electricity?

No. It is not clear that the statement that "any of those Parties that were short (and therefore could be said to causing the Demand Control)" is correct in all circumstances. It may be that there is a shortfall in area A, but due to system constraints etc., that the System Operator chooses to invoke Demand Control in area B and that Party X is short in area C. Given the system set up it could well be that Party X has not caused Demand Control to be invoked in area B, so should not be exposed to a higher SBP.

Furthermore we do not believe it is appropriate for the PSMG to consider (in respect of "Other Demand Control Offer Price Options") that "it would not reward Suppliers for what could be regarded as a market failure".

Firstly, why should Suppliers be "rewarded" for doing nothing? The choice of which GSP to be subject to Demand Control is chosen by the SO, without any involvement of Suppliers who thus take no action (to be 'rewarded'). It is appropriate that Suppliers are held neutral; i.e. do not incur costs (where Demand Control is invoked) for something they are not responsible for (being out of balance in a Demand Control area due to the action taken by the SO); but Suppliers should not receive a windfall profit; i.e. be rewarded; for these events. This issue (of rewarding a Supplier for doing

nothing) is compounded when it is noted (in respect of "Volume") "that the volume estimation would not reflect reality and....would not necessarily allocate demand reductions accurately", which is turn is exacerbated by the proposition that the volume allocation rules should be based on an "equivalent day" methodology. The worked example, where August 28th would be considered 'equivalent' to October 2nd, shows how inappropriate and inefficient this methodology would be.

Secondly, it is not clear that the market has failed (and, if it has, why are we not relying on the Section G Contingency arrangements) as the Demand Control could, for example, be invoked due to system problems. This is not a failure of the market, as there is no market for the system itself - we have only one System Operator.

Q3 Do you believe Proposed Modification P138 has a negative impact on Applicable BSC Objective (d) Promoting efficiency in the implementation and administration of the balancing and settlement arrangements

Yes. In addition to the reasons outlined in our response to Q1 and Q2 above we believe it would not be promoting efficiency in the implementation and administration of the balancing and settlement arrangements if the costs associated with this Modification Proposal were to be incurred as these costs do not outweigh the reputed benefits.

Q4 Overall, do you believe Proposed Modification P138 better facilitates the achievement of the Applicable BSC Objectives? Please give rationale and state objective(s)

No. For the reasons outlined in our response to Q1, Q2 and Q3 above.

Q5 Do you support the implementation approach described in the consultation document / the implementation option preferred by the Modification Group? Please give rationale

In respect of the "Demand Control Trigger", the suggestion that the end point should be determined as being the time the instruction was issued by the SO in accordance with OC6 (to begin restoring the demand) is not appropriate. There maybe sometime between the SO issuing an instruction (which may have a time lag built in) to the demand being restored to 'normal' (noting that historically when load is restored that circa 15% additional load 'returns' - if the load lost due to demand control is 100MW, then 115MW is the demand that comes back). It would be better if the end of the Demand Control period were determined as when the SO instruction has been carried out by the LDSO.

In regard to the comments that "the PSMG recognised that if other emergency measures were invoked.....these would override the P138 arrangements, effectively also constituting an end point to the Demand Control Period"; it is not clear what "Emergency Supply Arrangements, under the Electricity Supply Emergency Code" are. This needs to be clarified, as it is possible that provisions of the Electricity Supply Emergency Code (such as orders to certain users to reduce demand) could be on-going whilst OC6 Demand Control is invoked / underway).

Q6 Do you believe there are any alternative solutions that would better facilitate the Applicable BSC Objectives to a greater degree than P138 (for example, adopting P138 with one of the suggested alternative pricing options or any other options that the Modification Group has not

identified) that should be considered? Please give rationale

Q7 Do you agree with the PSMG's views of the scope of P138 in relation to those Parties covered / not covered by the modification (see page 3 of the consultation document)? Please give rationale

Q8 Does P138 raise any issues that you believe have not been identified so far and that should be progressed as part of the Assessment Procedure? Please give rationale

Q9 Are there any further comments on P138 that you wish to make?

We have nothing further to add at this time.

Regards

Garth Graham  
Scottish and Southern Energy plc